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NAFTA at 10:

An In-Depth Look at the Trade Agreement's Record
Serving Countries, Commodities and Consumers

The Magazine for Business Firms Selling U.S. Farm Products Overseas

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Features

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Ten Years of NAFTA Have Changed the Face of U.S.-Mexican-Canadian Trade

By Barbara Wojcik-Betancourt

On Jan. 1, 1994, Canada, Mexico and the United States began implementing NAFTA (the North American Free Trade Agreement). Even before implementation began, NAFTA was the subject of considerable speculation, encompassing everything from serious reservations to confidence in open and transparent markets.

Ten years of NAFTA have changed the face of U.S.-Canadian-Mexican trade, and this anniversary presents an opportunity to assess those changes. This issue of **AgExporter** examines NAFTA from several perspectives: its impacts on overall agricultural trends and various commodity sectors; its influence on foreign investment and market integration; and benefits for producers and consumers in the three signatory countries.

NAFTA is a groundbreaking agreement in several important ways, and has served as a good test for the workability and efficacy of trade liberalization. It created a free trade area among developed and developing economies. It is one of the first agreements to include agriculture as well as other industries.

NAFTA provisions include market access through TRQs (tariff-rate quotas), elimination of nontariff barriers through conversion to TRQs, grade and quality standards procedures, sanitary and phytosanitary regulations and rules of origin. A primary objective of NAFTA has been the complete elimination of barriers to trade among the three signatories. Many tariffs were dropped immediately; others have been or are being phased out. All agricultural provisions are to be implemented by 2008.

The agreement also established procedures for handling disputes and a nondiscrimination rule granting the trade partners the same treatment provided to nationals. To improve investment flows, each member must accord investors and investments from the other two countries the same treatment provided to its own citizens in all aspects of the investment process, from acquisition to management to disposition of investments.

While implementation has not always proceeded smoothly, and disputes continue to affect trade in some commodities, there is no doubt that NAFTA has had a significant impact on agricultural trade among the NAFTA partners. It has facilitated greater exports by increasing access to the U.S., Mexican and Canadian markets and by ensuring a climate of greater openness, stability and certainty for producers, importers, exporters and investors throughout the region.

Two-way agricultural trade between the United States and Mexico increased by more than 70 percent between calendar 1994 and 2002, when it reached $12.7 billion. Two-way agricultural trade between the United States and Canada grew more than 75 percent over the same period, reaching more than $19 billion in 2002.

While NAFTA is primarily concerned with trade, it has provided numerous intangible benefits as well. It has encouraged commitment to reforms and led to major advances in government procurement and intellectual property rights. Moreover, NAFTA was the first trade agreement to explicitly include environmental provisions. A side agreement–the North American Agreement on Environmental Cooperation–was developed to further address those concerns. ■

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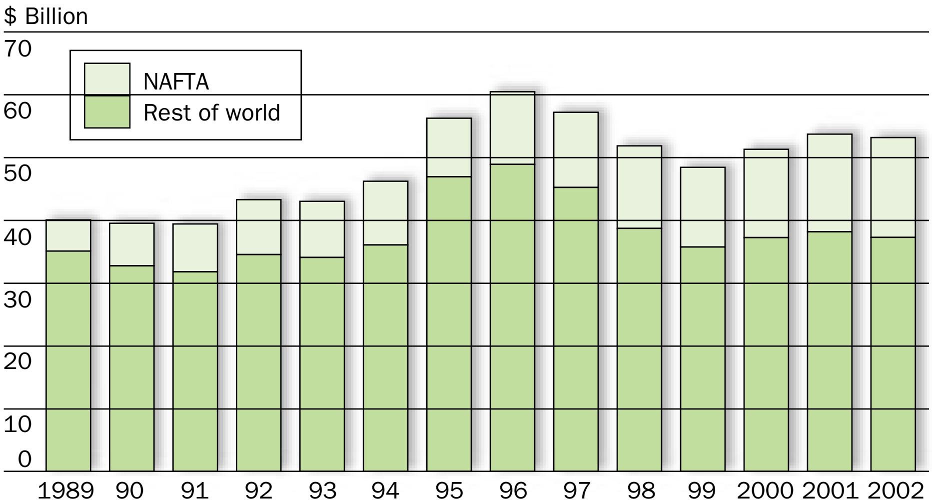
Charting the Progress of North American Trade

By *Barbara Wojcik-Betancourt*

U.S. Agricultural Exports to NAFTA Partners Have Grown Faster Than Exports to the Rest of the World

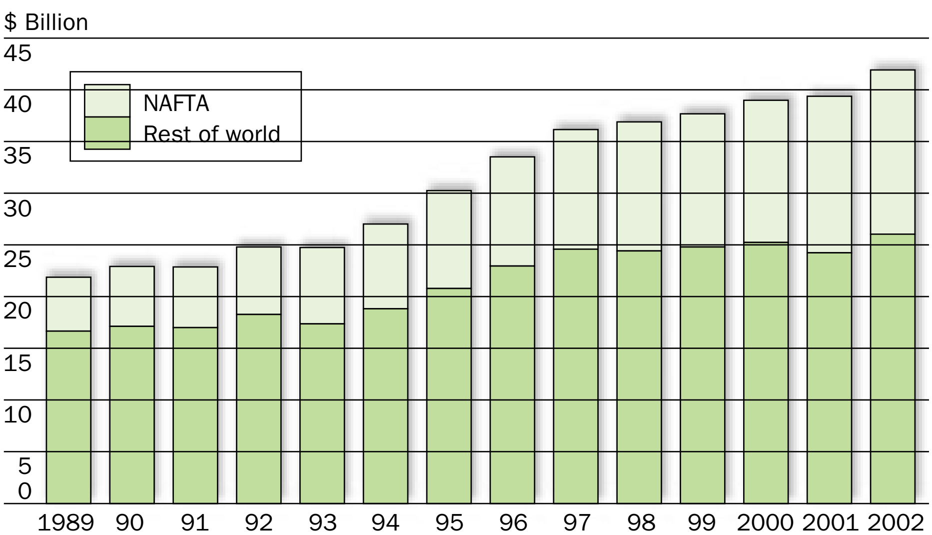
In 1989, U.S. exports to Canada and Mexico combined totaled $4.9 billion
In 1994, they were $10.1 billion
In 2002, they were $15.9 billion



Source: *Foreign Agricultural Trade of the United States,* USDA's Economic Research Service.

U.S. Agricultural Imports From NAFTA Partners Have Grown Apace as Well

In 1989, U.S. imports from Canada and Mexico combined totaled $5.2 billion
In 1994, they were $8.2 billion
In 2002, they were $15.9 billion



Source: *Foreign Agricultural Trade of the United States,* USDA's Economic Research Service.

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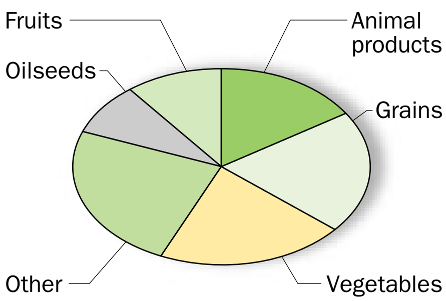
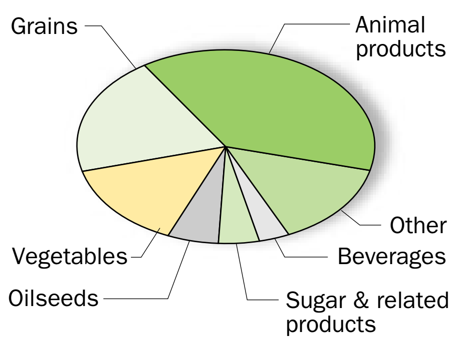
U.S.-Canadian Agricultural Trade in 2002



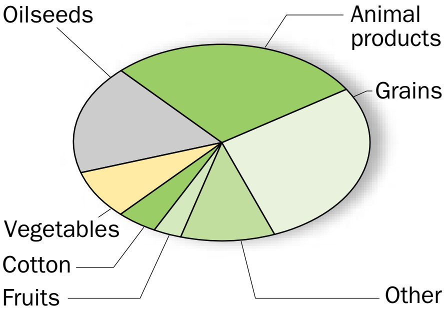
U.S. exports to Canada: $8.7 Billion



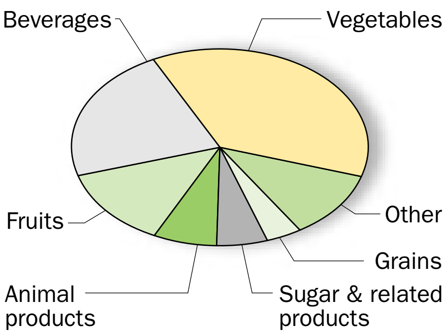
U.S. imports from Canada: $10.4 Billion

Source: U.S. Trade Internet System, www.fas.usda.gov/ustrade.

U.S.-Mexican Agricultural Trade in 2002



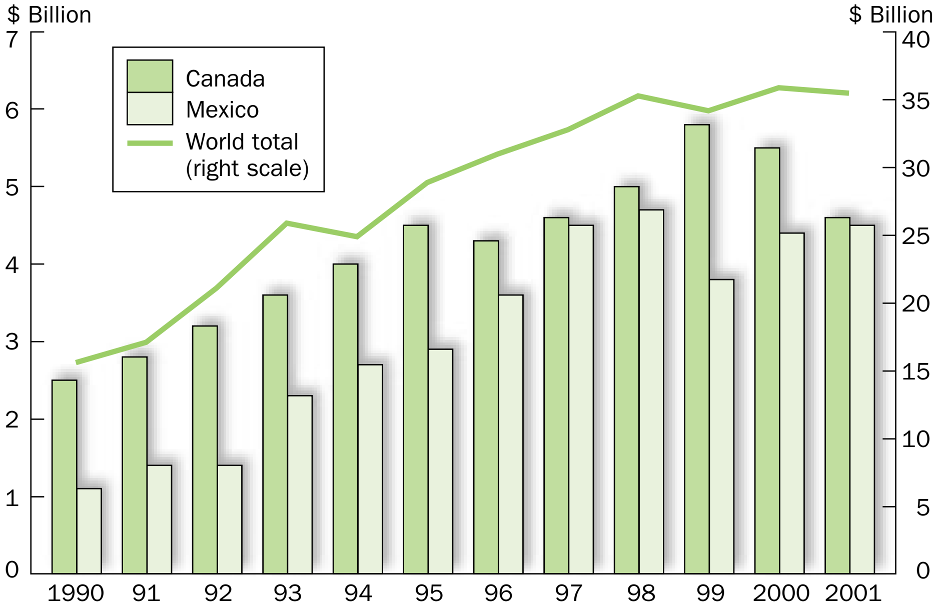
U.S. exports to Mexico: $7.2 Billion



U.S. imports from Mexico: $5.5 Billion

Source: U.S. Trade Internet System, www.fas.usda.gov/ustrade.

Since the Early 1990s, Growth in U.S. Investment in the Food Sectors of Canada and Mexico Has Mirrored Worldwide Investment of All Countries



Source: U.S. Dept. of Commerce, Bureau of Economic Analysis.

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Gauging NAFTA's Success and Confronting Future Challenges

By Thomas Vollrath

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NAFTA (the North American Free Trade Agreement) and its predecessor, the CFTA (U.S.-Canada Free Trade Agreement), were designed to make the North American market more efficient and thereby enhance the economic well-being of the United States, Canada and Mexico.

The principal means to achieve this objective was to foster integration of the three countries' markets by eliminating trade and investment barriers that interfered with fundamental economic forces and inhibited the international competitiveness of each NAFTA member.

Impetus for Market Integration

In a more integrated continental agricultural market, farmers are better able to specialize in production activities in which they are comparatively proficient; consumers enjoy lower prices for food; and society reaps rewards from increasing returns due to technological innovations and economies of scale. The benefits of integrated markets explain the creation of the Common Market and its expansion into today's EU (European Union), participation by many countries in regional trade agreements and the genesis of the General Agreement on Tariffs and Trade and its successor, the World Trade Organization.

Policy shifts and recent changes in the trade and investment record suggest that CFTA and NAFTA have contributed to the increased integration of North American agriculture. In addition to lowering tariffs or eliminating them altogether, the agreements converted many non-tariff barriers to tariff equivalents.

CFTA and NAFTA also accorded national treatment to foreign direct investment that triggered an avalanche of foreign capital into and out of the United States, Canada and Mexico. As a result of such investment, many large food corporations (i.e., Grupo Industrial Bimbo, Kraft, McCain Foods and PepsiCo) organized themselves as North American rather than national companies. Today, these conglomerates outsource many operations to take advantage of differences in production costs across member countries and to enhance their ability to respond to the demands of the enlarged continental market.

Explosive growth in the real value of agricultural trade within the NAFTA region (intra-NAFTA trade) also points to greater market integration in agriculture due to the free trade agreements.

Between 1987-88 and 2000-01, agricultural trade among the United States, Canada and Mexico increased 155 percent, surging from $11.2 billion to $28.6 billion in real (1989-91) terms. Data used in this analysis are derived from the Comtrade system of the United Nations. Of particular significance is that intra-regional export market shares grew faster than exports supplied by the United States, Canada and Mexico to countries outside NAFTA.

Clearly, North America has become an increasingly important market for U.S. agricultural exporters. Canada is now the largest importer of U.S. agricultural goods, displacing Japan in 2002. Mexico surpassed the EU as an export market for U.S. agriculture two years earlier.

Similarly, the United States is a very important market for agricultural exporters in Canada and Mexico. The share of Canadian exports absorbed by the United States climbed from 39 to 67 percent between 1991 and 2002. The share of Mexican agricultural exports destined for the United States is even higher, averaging 83 percent during the past decade.

Challenges and Paths to Progress

Despite the progress made, more could be done to deepen market integration within North America, as the continental market remains more segmented than the individual national economies of the United States, Canada and Mexico.

Prior to the implementation of CFTA and NAFTA, within-country trade was about 20 times larger than between-country trade in North America, after controlling for the influence of distance and market size. By 2000-01, within-country trade was about 12 times greater than between-country trade.

The discrepancy still remaining between internal and cross-border trade suggests that the North American market would become more efficient and better integrated if all noneconomic barriers inhibiting cross-border trade and investment were removed.

The major dilemma confronting the emergence of a truly unified North American economy is that, while product and input markets are becoming more integrated across international borders, the institutions to support this integration remain largely national. Harmonized product, health, safety and environmental standards have yet to be widely established, and contentious issues remain in such areas as dairy, beef, sugar, wheat, rice, corn, livestock, lumber, transportation and labor migration. Most agricultural disputes among the NAFTA countries stem from differences in national laws and regulations, divergent domestic farm programs and incompatible macroeconomic policies.

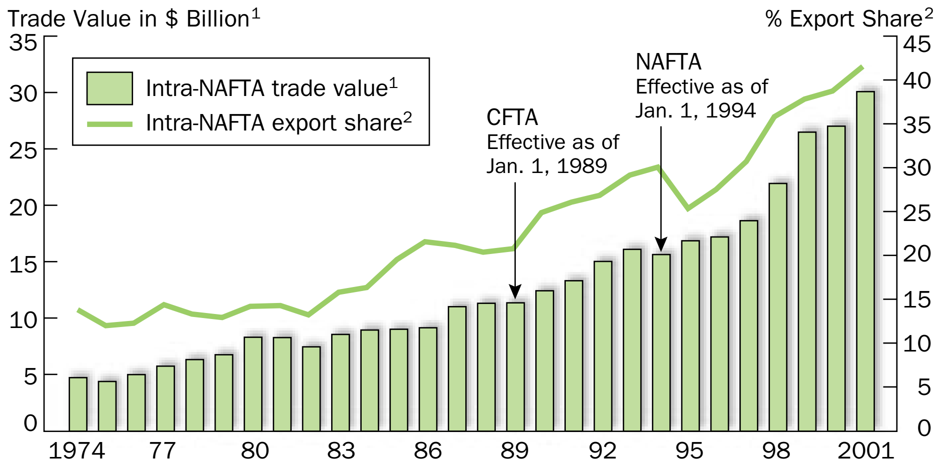
The policy agenda that must be addressed if further market integration is to take place within North American agriculture is likely to be more complex than the agenda that was agreed upon during the CFTA and NAFTA negotiations. A consensus about goals, guiding principles, and rules and procedures for handling disputes is essential.

All three NAFTA countries divide authority constitutionally between national and regional governments. The federal structure of member country governments creates challenges in forging a unity of purpose and devising policies that effectively and fairly address issues at the root of divisions.

One possible way to advance North American market integration is to enhance the influence of existing institutions: the NAFTA dispute resolution process, the various NAFTA committees (such as the Committee on Sanitary and Phytosanitary Measures) and informal working groups (such as those focused on migration, animal health and rules of origin). Another avenue is to create cross-border federal task forces charged with reaching agreement about how to resolve contentious problems in ways that incorporate common interests.

In the distant future, there is the possibility that supranational institutions will be created, whose members would represent the interests of the North American community and who would be endowed with the authority to negotiate policy with nationally chosen governmental officials.

Trade Shares Show That Intra-NAFTA Agricultural Trade Has Grown Faster Than NAFTA Partners' Trade With the Rest of the World



[1] Total value of U.S., Canadian and Mexican agricultural exports to (imports from) each other.
[2] Percent share of trade among the NAFTA partners compared with their exports to countries in the rest of the world. For example, in 2001, about 41.6% of the combined U.S., Canadian and Mexican trade took place among themselves, and about 58.4% of their trade was with countries outside NAFTA.
Source: ERS International Bilateral Agricultural Trade data derived from UN Comtrade deflated by FAOSTAT trade indices.

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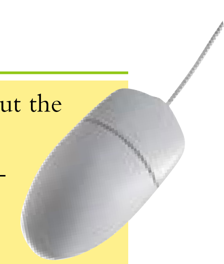
For further information about the integration of the U.S., Canadian and Mexican agricultural economies, see the report entitled "North American Agricultural Market Integration and Its Impact on the Food and Fiber System" on the ERS home page: **www.ers.usda.gov/publications/aib784/**



Achieving Market Integration

By Ronald D. Knutson and Rene Ochoa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NAFTA (the North American Free Trade Agreement) has done much to expand agricultural trade among the United States, Canada and Mexico. While trade has the effect of integrating our markets, much remains to be accomplished. Taking additional decisive steps to integrate markets could be the next phase for progress under NAFTA.

Market integration exists when product flows between countries are on the same terms and conditions as within countries. It implies that products can be traded between distinct markets or countries just as they are within a country. Price differences are no more than the cost of transportation plus related transaction costs. As a result, changes in supply or demand in one country affect the price and/or volume of transactions in the other.

Market integration is accomplished by private sector business activity, primarily through trade and foreign direct investment. The government's role is to remove obstacles to trade and foreign direct investment among countries.

Consequences of Market Integration

Market integration gives countries the advantages of competition and trade. U.S. consumers have enjoyed the benefits of lower cost blue jeans, fruits and vegetables as a result of integration between Mexican and U.S. markets. Market integration also means that common food production and marketing systems that ensure food safety and improve food security can be developed across countries.

However, market integration does not come without costs. Farmers in states such as California, Florida, Oregon, Michigan, Texas and Washington have had to adjust to supplies of Mexican fruits and vegetables entering the U.S. market. Likewise, U.S. farmers have been able to export more feed grains and livestock products to Mexico. At the same time, Mexican hog and poultry producers have had to adjust to increased supplies of meat imported from the United States. U.S. wheat and beef producers had have to adjust to integration of Canadian products. Yet time and again it has been demonstrated that the benefits of market integration weigh heavily on the plus side.

Under NAFTA, total U.S. trade with Mexico and Canada increased by 37 percent from 1993 to 2002, compared with 31.5 percent with the rest of the world. U.S. foreign direct investment in Canada more than doubled, while in Mexico it tripled. U.S. agricultural trade with Canada and Mexico almost doubled over the same period, while trade between Canada and Mexico grew more than 150 percent. Across the NAFTA countries, the mean annual growth rate for agricultural trade has exceeded 8 percent since 1990, the year after the U.S.-Canada Free Trade Agreement began to go into effect.

Facilitating Market Integration

Market integration should not be confused with a common market or an economic union, which both imply a significantly higher level of economic integration, such as a common currency under an economic union, and political integration, such as common farm programs. Market integration can be achieved without sacrificing national sovereignty to anywhere near the degree of economic integration characteristic of common markets and economic unions.

Facilitating market integration requires a commitment of governments and industry to define the required program adjustments and the strategies and timeline to achieve them.

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Developing Compatible Country Policies and Programs

Compatibility in areas such as product definitions, product quality, safety, security, inspection and traceability standards, labeling requirements and border measures and procedures contribute to market integration. Financial instruments such as payment procedures and requirements must also be compatible.

Achieving market integration requires administration, compliance and enforcement of programs in a manner that allows markets to be integrated. It is not unusual for the laws of other countries to be patterned after those of the United States. However, market integration is often deterred by the lack of consistent administration and enforcement of those laws.

Although NAFTA has demonstrated that much can be accomplished without compatible farm policies, ultimately the complex issue of compatible farm policies must be addressed. This requires sensitivity on the part of interest groups and policy makers to the realities that each country has relative advantages and disadvantages in production, processing and marketing. Domestic farm programs should not distort those relative advantages and disadvantages.

In other words, there must be a willingness to admit that one country can produce, process and market certain products more efficiently than another. The goal must be one of maximizing the advantages across countries through production, trade and foreign direct investment.

Vision and Resolve To Move Forward

The establishment of NAFTA was a first step in North American market integration, but several additional steps are needed to achieve full integration. Many of these steps involve individual country actions.

Likewise, the many rounds of multilateral trade negotiations, such as the current Doha Round of the World Trade Organization, have been designed to foster a higher level of market integration. Ultimately, the degree of integration achieved depends on individual countries pursuing and administering policies and programs consistent with this goal.

Globalization, one of the major forces affecting agriculture, implies that U.S. markets will continue to integrate with those of other countries. Like trade, market integration is a two-way street. The strength of U.S. agriculture, and that of other countries, lies in the application of technology to the commodities that it produces most efficiently and in trade and investment with countries throughout the world.

While once dependent on the sale of bulk commodities, in the era of market integration, U.S. farmers and agribusiness firms will be required make differentiated, value-added products available that are consistent with the desires of foreign consumers. ■

This article was prepared in conjunction with USDA's Economic Research Service. Knutson is professor emeritus and Ochoa is an international project coordinator at Texas A&M University, College Station, Texas. For more information, contact: Tel. (979) 845-5913; Fax: (979) 845-3140

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Canada and NAFTA: A 10-Year Measure of Success in Canadian-U.S. Agricultural Trade

By George C. Myles and Matthew Cahoon

It may not be obvious, but the United States and Canada have the world's largest bilateral trading relationship. In 2002, total trade between the two countries was $411 billion. Merchandise trade alone was $370 billion, translating into more than $1 billion in goods crossing the border each day. When services are added, the daily total equals $1.1 billion.

Sizing Up Canadian-U.S. Trade

Canada ships 87 percent of its merchandise trade exports to the United States, and receives 63 percent of the goods it imports from the United States. On the flip side, 23 percent of U.S. merchandise exports go to Canada, and 18 percent of the goods the United States imports come from Canada.

The agricultural provisions of the CFTA (U.S.-Canada Free Trade Agreement), which began taking effect in 1989, were incorporated into NAFTA (the North American Free Trade Agreement). All tariffs affecting agricultural trade between the United States and Canada, except for a few items covered by tariff-rate quotas, were removed by Jan. 1, 1998.

Agricultural trade with Canada has continued to flourish under NAFTA. As noted elsewhere, Canada is the No. 1 market for U.S. agricultural exports, purchasing $8.7 billion worth in calendar 2002, and exports were forecast to reach $9.4 billion in 2003. Since 1994, U.S.

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agricultural products to Canada have accounted for almost half of total growth in U.S. agricultural exports worldwide, and the growth rate has significantly outpaced that of sales to the rest of the world. The average annual growth rate of U.S. agricultural product exports to Canada since implementation of NAFTA was 5.1 percent, while that for the rest of the world was only 1 percent.

Two-way agricultural trade between the United States and Canada for 2003 was poised to reach $21 million, about double the 1994 figure, before the discovery of bovine spongiform encephalopathy in Canada last May. Subsequent emergency trade restrictions on U.S. imports of Canadian cattle and beef resulted in lower export values for two of Canada's leading agricultural exports.

A Sector-by-Sector Review

Although U.S. imports of Canadian agricultural products have grown under NAFTA, mostly of red meats, live animals and frozen potato fries, U.S. exports of a wide range of bulk, intermediate and consumer-oriented agricultural products to Canada registered significant gains. Without the trade agreements, the United States would have lost these expanded export opportunities.

Spurred by an increase in coarse grain exports, U.S. bulk commodity exports to Canada for 1994-2003 increased at an annual average of more than 10 percent, creating a $1.0 billion market. U.S. intermediate exports rose more than $500 million. U.S. high-value food exports grew at an annual average rate of 4.5 percent and have created a stable $6.0 billion market for U.S. manufactured consumer food products.

Besides the market opportunities created by zero tariffs, NAFTA has given Canadian consumers greater freedom to determine the demand for high-value agricultural products in a more competitive marketplace. Canada's wholesale, retail and food service industries are watching with acute interest developments in U.S. packaged and processed foods and service trends. Canadians learn about new and innovative U.S. food products about as soon as U.S. consumers do via the media and frequent business and personal travel to the United States. These information sources create an immediate demand that helps ensure the success of U.S. high-value food products.

As demand accelerates and two-way trade expands, food policy makers in Canada recognize the importance of working with the NAFTA partners toward harmonization in food packaging and nutrition labeling regulations. These developments promise further impetus for accelerated trade for the NAFTA partners in the coming years.

Good Produce Makes Good Neighbors: Under the tariff phase-out provisions of NAFTA, U.S. fresh vegetable exports to Canada enter duty-free; seasonal duties are no longer applicable. Although a tariff snapback provision remains in effect until 2008, it has been used sparingly by Canada, and not at all in recent years.

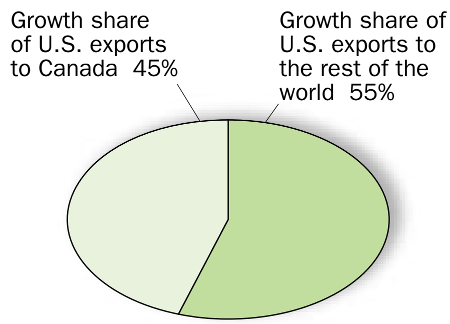
NAFTA has enabled U.S. fresh vegetable exporters to benefit from the expanding opportunities in the Canadian market, stemming from increased demand in the food service sector and higher fresh market sales to Canada's growing number of Asian immigrants, whose traditional diet includes large amounts of fresh vegetables. Canada has one of the world's highest consumption rates of fresh vegetables. In Canadian retail grocery stores, more space is devoted to fresh produce than to any other food sector.

U.S. fresh vegetable sales to Canada reached $964 million in 2002 and posted an annual average growth rate of 4.2 percent since NAFTA implementation. Sales were set to exceed $1.0 billion in 2003, making Canada the No. 1 market for U.S. exports in this product category. NAFTA border facilitation measures and modern transportation and wholesale dealer networks provide Canadian fresh vegetable buyers with prompt delivery.

The Chicken and the Egg: Prior to the trade agreements, Canada imposed specific import controls on all major poultry and egg product trade. U.S. exports were restricted to quotas based on the previous five-year historical access level. Under the CFTA and NAFTA, U.S. negotiators increased access to fixed percentages of Canadian production of the products, thus enabling exports to grow as the market expanded.

In January 1995, the Uruguay Round of the General Agreement on Tariffs and Trade was implemented, and Canada converted its import protection for poultry to a TRQ (tariff-rate quota) system. The Canadian government honored its NAFTA commitment, whereby U.S. access was higher than Canada's minimum access requirements under the Uruguay Round provisions.

For 1994-2002, Growth in U.S. Agricultural Exports to Canada Mirrored Worldwide Increases



U.S. negotiators had insisted that certain processed poultry items be exempt from Canada's list of items included in the poultry meat TRQ, and in recent years, U.S. exports of these items have increased. In addition, the Canadian government was obliged to establish special supplementary import categories to enable Canadian food manufacturers who use poultry meat ingredients to import additional U.S. poultry meat, in order to improve their competitiveness with similar products of U.S. manufacture that enter Canada duty-free under NAFTA.

These factors have resulted in steady and substantial growth in U.S. poultry meat exports that may not have occurred without NAFTA. Today, Canada is the No. 2 export market for U.S. chicken. Total U.S. poultry exports to Canada in 2003 are estimated at about $290 million, a 77-percent gain over the pre-NAFTA level.

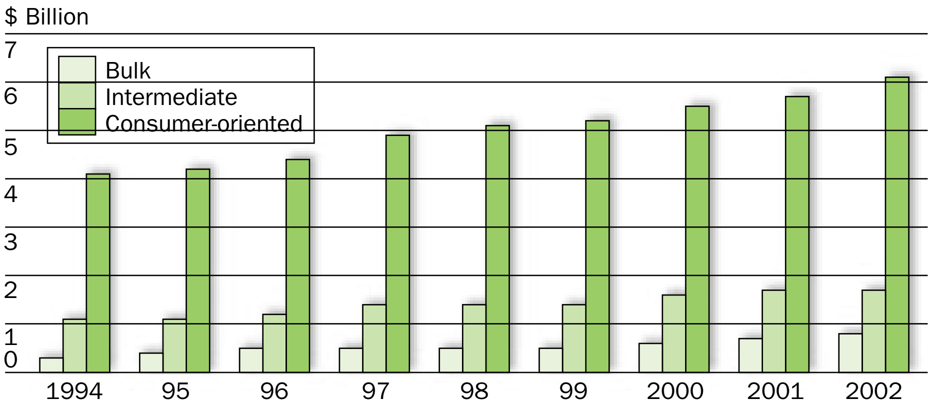
Dairy Products Tending Upward: Implementation of the Uruguay Round provisions one year after NAFTA saw Canada's import control regime switch from a system of import quotas to a TRQ system in order to protect Canada's fluid milk production. TRQs were established for fluid milk and dairy products, including yogurt, powdered whey, specialty creams, dairy spreads, ice cream and ice cream novelties, cheeses, butter and margarine. Under the TRQ system, imports are subject to low duty rates up to the limit, and to higher rates over the limit.

Despite the high tariff rates on over-quota volumes and the creation of certain value-added dairy products that were either excluded from the list of products to which a TRQ would apply or have been developed since the conversion from quotas to TRQs, U.S. exports of dairy and dairy-containing products to Canada have more than tripled. For 1994, U.S. exports totaled $75.9 million; for 2002, they were $254.6 million. Leading U.S. exports in this sector include preparations for infant use (containing over 10 percent by weight of milk solids), pizza and quiche, dry whey, milk albumins/whey protein concentrates, milk-based drinks and processed cheeses.

Livestock and Grain Gains: Cross-border trade and investment increased under the trade agreements. U.S. grain corn shipments to Canada benefited as the U.S. and Canadian livestock industries became more integrated. As market integration advanced, Canadian livestock numbers grew.

Despite increases in Canada's planted corn area, U.S. corn sales rose sharply to meet feed grain demand. In 2002, western provinces accounted for the majority of U.S. corn sales in Canada. Rising demand for corn for industrial purposes, namely ethanol and sweetener production, outstripped supply in Canada's traditional

Exports of U.S. Consumer-Oriented Products Lead NAFTA Sales Growth to Canada



eastern corn-growing region. In 2002, U.S. grain corn exports reached 4.0 million metric tons valued at $395 million, more than five times their value when NAFTA was first implemented.

Pet Foods Popular: The pre-CFTA/NAFTA tariff on U.S. pet foods for dogs and cats was 6 percent ad valorem. Under NAFTA, U.S. pet food manufacturers have seized opportunities to benefit from a decade-long Canadian boom in pet ownership through increased pet food sales and investments. In recent years, several familiar pet superstores have set up retailing operations in Canada's major cities, and all carry the major U.S. brands. Canadians currently own about 8 million dogs and cats. Total retail sales (food, accessory and veterinary costs) are expected to exceed $1.5 billion in 2003. U.S. pet food sales to Canada have surged by 40 percent under NAFTA, reaching $275 million in 2003.

Snack Food Sales Swell: Before 1989, Canada applied moderately high tariffs, mostly 5-10 percent, on imports of U.S. salty snacks (popcorn, corn chips, potato chips and pretzels) and bakery snack foods (crisp breads, cookies, waffles and wafers). In general, an ascending scale typified the tariff-rate structure—the more processed the item, the higher the import duty to protect domestic manufacturers.

Under NAFTA, Canada's snack food industry has become highly concentrated, and now includes national, regional and multinational firms. It is estimated that the leading four enterprises supply over 85 percent of total Canadian snack food production. Canada's snack food industry primarily serves the domestic market. Prior to the CFTA, imports supplied about 3.2 percent of the domestic market. Although Canadian companies continue to hold a substantial portion of the snack food market, imports, mostly from the United States, have captured about 15 percent of it.

With Canada's snack food industry invigorated by the trade agreement provisions, Canadian demand also rose for key commodity inputs needed to make snacks. While many of these products, such as potatoes and oil, are supplied by domestic sources, demand has increased for many other U.S. inputs (corn meal, seasonings, etc.), reflecting the economic multiplier effect of freer trade. Imports of snack foods (excluding nuts) from the United States in 2003 are expected to have reached a record $725 million.

Canada's Perspective

How has NAFTA worked for Canada? According to Canada's Department of Foreign Affairs and International Trade, NAFTA has brought economic growth and rising standards of living for people in Canada, the United States and Mexico. The Canadian department claims that NAFTA has established a strong foundation for future growth and set a valuable example of the benefits of trade liberalization.

NAFTA is the world's largest trade bloc, with a gross domestic product of $11.4 trillion, about one-third of the world's total. Each day, NAFTA member countries conduct nearly $1.7 billion in trilateral trade. Thanks largely to NAFTA, North America is one of the most competitive, prosperous and economically integrated regions in the world.

From 1993 to 2001, Canada's merchandise exports to its NAFTA partners climbed 95 percent, from $117 billion in 1993 to $229 billion in 2001. By contrast, Canadian exports to the rest of the world in the period increased only 5 percent. During the first seven years of NAFTA, annual foreign direct investment in Canada averaged $21.4 billion, almost four times the average registered over the seven years preceding NAFTA. ■

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Mexico's NAFTA Experience

By David Williams

The public discourse on NAFTA (the North American Free Trade Agreement) too often focuses on the losers in free trade. The winners—and there are many, such as consumers in all three member countries—may not realize the important gains they have made. Free trade has generated broad growth. Sectors that have adapted and adjusted to the new trade environment, such as the automotive and electrical industries, are competing extraordinarily well. Those that cannot adjust are falling behind. In short, the first decade of NAFTA trade, particularly agricultural trade, has followed classic market-opening dynamics.

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And Speaking of Gains ...

Broadly speaking, NAFTA has been good for Mexico. Total two-way trade between Mexico and the United States grew from $81 billion in calendar 1993 to $231 billion in 2002, and Mexico steadily turned a modest trade deficit into a $37 billion trade surplus.

Mexico's exports to all countries grew 80 percent between 1985 and 1993, following its accession to the GATT (General Agreement on Tariffs and Trade, forerunner of the World Trade Organization), and that growth rate has nearly doubled since the inception of NAFTA. Its exports of manufactured products account for nearly 90 percent of total exports, and it's estimated that higher paying (37 percent higher on average) export jobs account for just over one in five jobs in Mexico.

Its annual growth in GDP (gross domestic product) averaged 5.4 percent from 1996 to 2000, well above the average of 3.9 percent from 1990 to 1994. Most analysts agree that exports were a key factor in accelerating Mexico's recovery from the 1995 financial crisis. GDP growth slowed considerably in 2001 and 2002, due in part to U.S. economic woes, but growth improved in the latter part of 2002.

Mexico's agricultural exports have also benefited from NAFTA. While Mexico has run a consistent annual deficit of around $1.5 billion with the United States, its agricultural exports to the United States have nearly doubled since NAFTA's inception, and were up 9 percent through August 2003 from a year earlier. Freer trade and increased competition have helped provide lower cost inputs for Mexico's livestock and food processing industries. Lower rates of inflation for food products have played a key role in stabilizing overall inflation since 1994.

Despite the increased competition, the dollar value of Mexico's total agricultural production in 2001 was 50 percent higher than in 1993 as production of key products rose, such as pork (up 24 percent), beef (13 percent), chicken (60 percent), sorghum (85 percent), fruits (27 percent) and vegetables (36 percent).

Many Mexican sectors are already very competitive with those of the United

States, such as tomatoes, avocados, live cattle, fresh fruits and vegetables. A key success story has been in exports of horticultural products (generally labor-intensive crops that can be grown profitably on smaller farms), which have increased by nearly 120 percent.

Structural Problems and the Debate in Mexican Agriculture

The Mexican agriculture debate, in which some have called for a renegotiation of NAFTA and more protection from imports, has been driven by opposition parties seeking to capitalize on long-standing political relationships with the rural poor. NAFTA provisions (particularly the elimination of most remaining tariffs and quotas on Jan. 1, 2003), coupled with the U.S. Farm Bill (Farm Security and Rural Investment Act of 2002), often have been portrayed as portending certain doom for Mexico's agricultural sector.

However, U.S. producers absorb costs that Mexican producers do not, such as high labor costs, costs of compliance with strict environmental and worker safety regulations and taxes. Moreover, the main difficulty facing Mexican agriculture is a number of structural problems. These problems are independent of, and cannot be addressed by, NAFTA.

About 22 percent of Mexico's labor force works in agriculture, which generates only 4.4 percent of GDP. Nearly 80 percent of producers are involved in the production of grains, legumes and oilseeds–Mexico's least profitable crops. About 50 percent of Mexico's farmers till plots of 5 hectares or less (1 hectare=2.471 acres), and they earn less than a third of their income from agriculture. NAFTA-generated jobs, stable inflation rates and lower consumer prices have helped these farmers reduce their dependence on agriculture.

Economic transition away from agriculture is inevitable for many small-scale agricultural producers. Future policies should focus on generating off-farm employment for those who need it, improving trade opportunities for the 15 percent of Mexico's producers who are globally competitive and improving the productivity of the 35 percent who have the potential to compete.

Strategies and Solutions

To address concerns on both sides of the border, the U.S. and Mexican governments and industries have maintained an open and active dialog to come up with solutions consistent with NAFTA. Examples of recent successful cooperation include the suspension of U.S. anti-dumping duties on Mexican tomatoes, better U.S. access for Mexican avocados, the signing of a poultry safeguard agreement and the lifting of Mexican anti-dumping duties on U.S. live hogs.

Mexico implemented important reforms during the 1990s, such as the elimination of price supports and public participation in the procurement and sale of commodities and inputs. Additionally, the government of Mexico established the PROCAMPO subsidy program for producers of basic crops and the Alliance for the Countryside Program, which provides matching grants for productive investments.

To help alleviate the political pressure from rural action groups, the government signed the Acuerdo (National Agriculture Agreement), which provides for an emergency spending fund, studies of the effects of NAFTA and the U.S. Farm Bill, a commitment to seek consultations with the United States and Canada on NAFTA provisions for white corn and dry beans (which have certain trade protections through Jan. 1, 2008) and other programs to raise the standard of living in rural areas.

The United States is working to forge commercial linkages between U.S. and Mexican companies. A key element in this strategy is the Partnership for Prosperity Program, which commits both governments to support activities such as trade missions and seminars to bring businesses together. USDA supported a mission of U.S. buyers to Mexico to link them with Mexican exporters, and is working to identify potential new-to-market exporters.

While some sectors have had challenges with liberalizing markets, NAFTA has offered a reasonable implementation period to allow countries to adjust to the changing market conditions.

NAFTA has been so good for Mexico that fully 20 percent of its GDP is now attributable to trade made possible by NAFTA provisions. NAFTA has benefited the Mexican rural as well as urban workforce by creating thousands of new, higher paying export manufacturing jobs.

Government of Mexico data indicate that poverty rates in both rural and urban areas have dropped since the economic recovery in 1996. A key lesson to be learned from NAFTA is that free trade will likely accelerate the economic transition to manufacturing and competitive sectors as resources are allocated more efficiently. ■

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NAFTA: A Win-Win Proposition for U.S. Producers

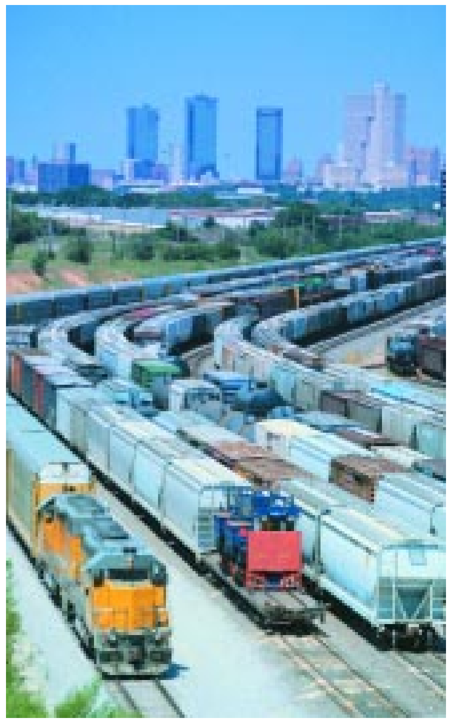
To get an overall picture of how well NAFTA (the North American Free Trade Agreement) has worked, **AgExporter** *interviewed Michael Dwyer, chief economist with FAS' Commodity and Marketing Programs area. Here are his insights on NAFTA's overall impact on U.S. agricultural trade, and on the economic fundamentals and comparative advantages that will shape future commerce trends among the three partners.*

AgExporter: What do you think NAFTA has done for U.S. agricultural trade with Canada and Mexico? How do you see its future?

Michael Dwyer: While there have been bumps in the road, a review of the past 10 years shows that NAFTA's success has been quite remarkable for U.S. agriculture. Overall, worldwide U.S. agricultural exports rose by about $6.9 billion between 1994 and 2002. Of that, $5.8 billion has been to Canada and Mexico. It's hard to overlook those statistics. With fewer trade barriers and food demand continuing to expand, particularly in Mexico, the future of U.S. exports to our NAFTA partners also looks outstanding.

Since 1994, Canada and Mexico have been our two top growth markets in the world–by a wide margin. Exports to Canada rose by about $3.1 billion over those years, while sales to Mexico rose about $2.7 billion. U.S. exports to the rest of the world rose by only $1.1 billion.

In the case of Canada, 70 percent of our exports are in the consumer-oriented HVP (high-value product) category. This



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includes horticultural products, meat and dairy products, snack foods, beverages and other grocery products. Corn and soybeans are the main export items in the smaller bulk commodity category. Most of these products have grown sharply since the U.S.-Canada Free Trade Agreement and NAFTA were signed. In fact, exports of many items are currently at record highs.

Exports to Mexico are more diversified than they are to Canada–with 39 percent being bulk commodities, 39 percent consumer-oriented HVPs and 22 percent intermediate HVPs (semi-processed products). Mexico is one of our largest export markets for each category. Growth in corn, soybean and wheat exports has done particularly well. Growth in cotton sales to Mexico has also been very impressive, due to the country's rising consumer and export demand for its textiles and apparel.

However, the biggest surprise has been the strong growth of many of our consumer-oriented HVPs to Mexico. Before NAFTA, U.S. exports of these products were severely limited by trade barriers and weak demand. Today, courtesy of the lower market access barriers and more vibrant Mexican economy that have resulted from NAFTA, Mexico ranks as one of our top export markets for a wide range of HVPs, including meats, fresh and processed horticultural products, pet foods and grocery products.

An interesting angle on the NAFTA success story concerns our market share in both Canada and Mexico. From the 1990s up until recently, our share of world agricultural trade had been slipping. However, thanks to the increased competitiveness of U.S. exports brought about by the reduction in market access barriers, our market shares in Canada and Mexico have grown, while our shares in most of our other major markets fell. Our share of Canada's agricultural imports has climbed to 65 percent, and our share of Mexico's imports is 75 percent. This means 75 cents of every dollar's worth of Mexican imports of agricultural products comes from the United States–up from 70 percent a decade ago.

AgExporter: What are the demand fundamentals likely to be?

Dwyer: They continue to look promising. Real economic growth in Canada is projected at roughly 3 to 3.5 percent a year over the next 10 years. The Mexican economy is expected to grow by 4 to 4.5 percent a year as the country continues to industrialize, benefiting from foreign investment inflows and trade liberalization. As Canadian and Mexican incomes grow, their food demand responds. This is particularly true in Mexico, where food demand is more sensitive to changes in income than in a more mature market like Canada.

In addition to these income gains, there are issues related to population and demographics. Mexico has a population of 105 million, and it is expanding by 1.5 to 2 percent a year. Mexico's middle class is expanding even faster, which is an important demand determinant with implications for the types of foods consumed–a greater emphasis on meats, fruits and processed foods. Canada has 32 million people, but its population is only growing by 0.5 percent a year. In Canada's case, most of the increases in food demand are coming from income growth and the accompanying increase in the demand for more healthful and upscale food products.

These demand factors, coupled with fewer market access barriers, mean consumers in both countries will want and will have increased access to the same U.S.-made food products as American consumers. These factors benefit most products but will particularly favor consumer-oriented HVPs, which include most of the fastest growing exports to Canada and Mexico over the past 10 years. And I see no reason why that trend would change as we move forward.

AgExporter: What role have exchange rates played in U.S. agricultural trade?

Dwyer: That's one of the most telling signs of how well NAFTA has benefited U.S. exports since it was signed. Up until recently, the U.S. dollar had been very strong against the world's major currencies. This hurt the competitiveness of U.S. exports, vis-à-vis those of other suppliers, and was one of the main reasons why U.S. exports to non-NAFTA countries have not performed the way we would have liked.

Yet exports have exploded to Canada and Mexico, whose currencies, until recently, had also weakened against the dollar. Why the difference in trade performance? I believe it shows that the benefits of trade liberalization–the reduction of trade barriers facing U.S. goods–have outweighed the trade losses to American exporters that come from a strong U.S. currency. If the dollar weakens further against the Canadian dollar and Mexican peso, the value of the dollar will go from a factor restraining our export performance to our NAFTA partners to one that is more supportive. This, combined with reduced trade barriers and growing food demand, creates an environment that is conducive to export expansion.

While the growth of exports to Canada and Mexico over the next 10 years will be hard pressed to match the impressive growth of the past decade, we expect that it will continue to exceed that to the rest of the world.

AgExporter: How would you rate NAFTA's effectiveness?

Dwyer: Any trade agreement is going to have trade issues. As barriers come down and U.S. products move in greater volumes into our partners' markets, it increases pressure on their producers who may have a harder time keeping up with the competitiveness of U.S. producers. It is naïve to think those producers won't pressure their governments to intervene and protect them. We've seen it used against us time and again. It happens to various degrees in all countries, even here.

However, the test of any trade agreement is whether the needs of the many are considered when you are trying to protect the few. In the case of NAFTA, U.S. consumers have benefited immensely by the more open trading relationship we have with Canada and Mexico. They have access to more food and agricultural

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products at good prices, just as consumers in Canada and Mexico benefit from NAFTA through greater access to U.S. products. Consumer welfare in all three countries has benefited from the trade agreement.

Have U.S. producers and processors benefited from reduction in trade barriers? For the most part, yes, although clearly there are some who have found the increase in import competition more challenging than others. As discussed earlier, the evidence is pretty compelling that U.S. producers and processors have seen substantial export gains from NAFTA. The significant and broad-based increases in U.S. exports to Canada and Mexico since 1994 stand in stark contrast to the situation for U.S. exports to many of our other major markets, which experienced declines during this period.

But some ask whether NAFTA has resulted in a flood of imports. That's a fair question. After all, the data clearly show that imports from Canada and Mexico have grown sharply since 1994. However, I would argue much of that increase is not due to the trade liberalization effects of NAFTA. First, U.S. imports from other countries over the same period of time rose sharply as well–so increases from Canada and Mexico were not unique. Second, in an aggregate sense, U.S. import barriers were already low prior to NAFTA, so the incremental change after NAFTA was not sufficient to generate significant import surges.

A better explanation for the increased imports from Canada and Mexico, and other countries for that matter, involves macroeconomic conditions. The strong dollar, the strong U.S. economy, and weak economic conditions in much of the rest of the world combined to make the United States an attractive market for most foreign suppliers.

If NAFTA is any indication of what can happen from a free trade agreement, it should encourage U.S. producers to be more willing to pursue trade agreements with other trade partners. Instead of fearing the increased competition, focus on the increased opportunity that these agreements present. We have and will continue to carry out export programs such as market development, export credit guarantees and other trade expansion activities at USDA to help increase U.S. exports. However, for the United States, which enjoys significant cost-of-production advantages in a wide range of food and agricultural sectors, nothing can generate the kind of export gains that trade liberalization can.

AgExporter: In discussing demand fun damentals, you mentioned economic growth as an important factor. Can you explain further how this affects U.S. food exports?

Dwyer: The Mexican economy is growing by roughly 4 to 4.5 percent a year, generating more jobs and increased discretionary incomes. This allows consumers to improve the quantity, quality and diversity of their diets. With import barriers facing U.S. products substantially reduced from pre-NAFTA days, U.S. producers can more effectively compete with both Mexican firms and third-country suppliers for Mexico's growing consumer demand. That's what we have been successfully doing since 1994, and I see no reason that will not continue in the years ahead.

To some degree, the same holds true for Canada. Obviously, the income levels in Mexico and Canada are quite different. We don't expect to see growth in Canadian demand approximate that of Mexico. It's a more mature market for most products. However, some sectors are more mature than others. The fastest growing component of Canadian food demand is fruit, vegetable and processed grocery products, which helps explain why U.S. exports of these products to Canada have done so well over the past decade. The Canadian diet, like the U.S. diet, is putting increased emphasis on fruits and vegetables. We have a much broader diversity of horticultural production than Canada does, and we are the supplier of first choice for those products as well as for processed products.

AgExporter: Do Canada and Mexico buy a lot of inputs from us for their food processing industries?

Dwyer: Yes. One of our major agricultural exports is food ingredients. That's not just true of NAFTA, that's true on a global scale. It's truly been one of our export success stories over the last 10-15 years. The bottom line is the global processed food market is booming. Because we have such a productive food ingredient market and large production capability, we are the leading exporter, with the European Union a close second.

AgExporter: Is demand changing U.S. production and processing?

Dwyer: The demographic changes that are driving the U.S. food market also are driving the larger global market. With more people working and less time to prepare traditional meals, there's greater demand for ready-to-eat foods. There's

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also an increased emphasis on products' healthful characteristics.

These demographics are at play in Canada and to a lesser degree in Mexico. Although per capita incomes in Mexico tend to be much lower than our own, there are growing numbers of two-income households. This means two things. First, two-income households have less time to spend making traditional meals, so there's greater demand for convenience foods. Second, household incomes are much greater than per capita levels, so there's a greater ability to afford those convenience foods. These households tend to be in urban areas. Urban areas have more wealth and purchasing power than rural areas. That's where the majority of well-paying jobs are.

AgExporter: Those areas also have the infrastructure to support imports—cold storage, transportation and distribution.

Dwyer: That's right. Ownership of refrigerators is higher in urban areas because income levels are greater. Per capita ownership rates of microwave ovens, refrigerators, air conditioners, televisions—all those types of things—are growing over time. Those are good leading indicators. You can't sell perishable fresh and frozen foods unless households have refrigerators.

I think what's interesting is the growth of supermarkets. To a great degree it explains how U.S. processed food products are growing so rapidly in Mexico, in Central America and in Latin America. The growth of the supermarket as a retailing outlet versus the traditional mom-'n'-pop store is driving international trade in consumer-oriented HVPs.

There's been a fair amount of research done on the companies doing this retailing, and they are the same company names that are familiar in the United States, such as Wal-Mart and Ahold. The large food retailers are going global, and as barriers to trade come down, the economics are determining where the investment and trade take place.

Many times the standards of these food retailers are higher than the standards of the governments enforcing them. In other words, a supermarket retailer's standards for food quality and safety may well be higher than those of the country in which it operates. If the retailer is a large enough buyer, it can set the terms of its purchases from local and international suppliers. If local suppliers cannot meet the minimum threshold standards, that retailer will import to ensure the products meet certain corporate standards. This is happening all over the world.

AgExporter: Is this growth also happening with convenience stores, such as gas marts?

Dwyer: Convenience stores have a more prominent retailing role in many other countries than they do here. Typically we do most of our grocery shopping at large supermarkets, and do only impromptu, spontaneous purchases from convenience stores and gas marts. But in Asia and in Mexico, these kinds of markets account for a larger percentage of every food retail dollar.

AgExporter: Will there be a lot more international investments in other countries?

Dwyer: I think you can pretty much bank on that. Most of the growth for global supermarket chains will occur outside their home bases, mostly in a handful of rapidly growing developing countries. Certainly, this is true in Mexico, but China, South Korea and Indonesia, where food demand is rising rapidly, are also good candidates. Trade liberalization allows for greater competition, which makes this story more compelling for well-managed U.S. producers and processors. ■

The Canadian Furniture Industry Presents Opportunities for U.S. Hardwoods

By Lashonda McLeod

U.S. exports of hardwood logs, lumber and veneer to Canada increased steadily over the last decade since NAFTA (the North American Free Trade Agreement) went into effect. Expanding furniture production in Canada has fueled these exports. Canadian furniture manufacturers are becoming more dependent on U.S. hardwoods.

NAFTA provides incentives for buying within the North American region and ensures that North American producers receive the primary benefits of all newly established tariff preferences. Because of NAFTA, U.S. hardwood lumber exports to Canada increased from $246 million in 1995 to $347.5 million in 2002. The United States is Canada's No. 1 source of hardwood lumber. In 2002, the U.S. share of Canadian imports was 95 percent. Canada's hardwood lumber imports exceed its domestic production. Canada re-exports U.S. hardwood lumber to other markets in the form of Canadian furniture.

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Status of the Furniture Industry

Canada produces a wide array of furniture products for the world market. In 2002, Canada exported $3.7 billon worth of residential, office and institutional furniture to the United States.

The Canadian furniture industry has undergone substantial consolidation during the past 10 years. The number of furniture manufacturing plants decreased by 32 percent between 1990 and 1999, from 2,571 to 1,748. However, total employment and average establishment size grew, 56 percent and 69 percent, respectively. Production is composed of household furniture (including mattresses), office and institutional furniture, kitchen cabinets, counter tops and other manufactured products.

Exports have been an engine for growth as Canadian furniture exports increased by 383 percent between 1992 and 2001, including substantial export growth to the United States.

The province of Quebec has a vibrant hardwood lumber and processing industry using both domestic and imported woods. In 1999, Quebec furniture industry shipments amounted to $2.0 billion. Approximately half of that was destined for export. Canadian furniture manufac-

LARGELY BECAUSE OF NAFTA, U.S. HARDWOOD LUMBER EXPORTS TO CANADA ROSE FROM $246 MILLION IN 1995 TO $347.5 MILLION IN 2002.

turers export most of their products to the United States and the European Union. Quebec's furniture industry export orientation increased dramatically between 1991 and 1999.

Export Opportunities for U.S. Firms

Canada's furniture industry has grown despite consolidation in the sector. Growth was fueled by housing starts, growing nonresidential construction, growth in home renovations and record low interest rates. The booming housing market has led to increased employment in the furniture manufacturing industry and increased demand for furniture.

NAFTA provides an incentive for Canadian furniture manufacturers who re-export their products to the United States and Mexico. Under NAFTA rules of origin, goods that originate in Canada, Mexico or the United States gain duty-free access to the U.S. market.

For example, a wooden chair manufactured and assembled in Canada from a combination of NAFTA-originating and non-NAFTA-originating components can be considered to be a NAFTA product if the chair meets the specific rules of origin. If all materials and components were sourced from a NAFTA country, the chair qualifies as NAFTA-originating, and no duties would be owed.

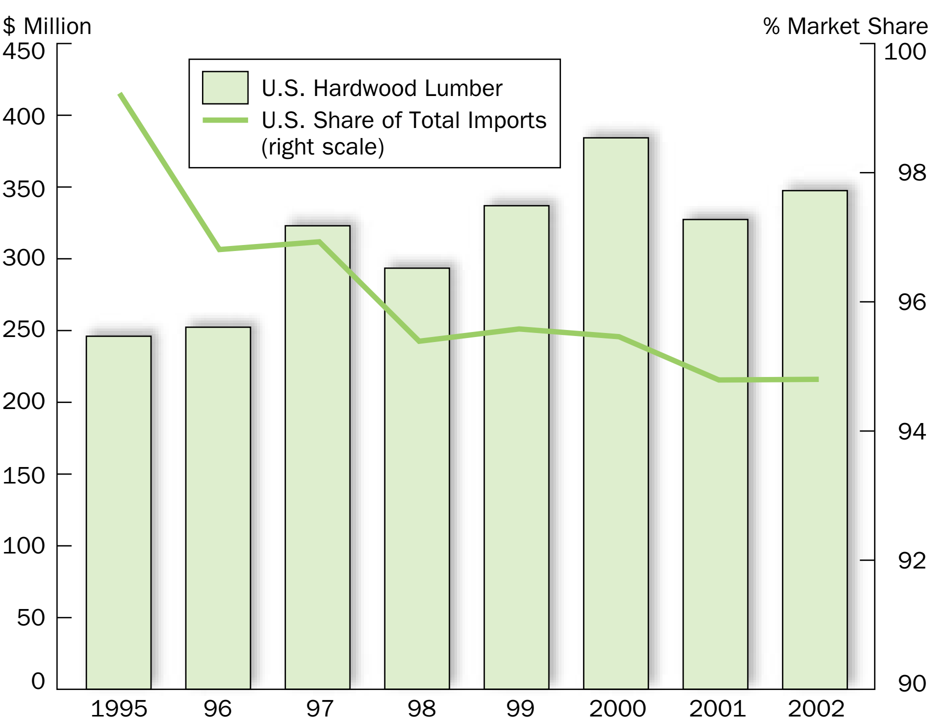
Canada's household furniture industry is known for transforming value-added materials, such as hardwood lumber, into finished consumer goods. Its primary strength is wooden furniture production. Moreover, U.S. household furniture products such as home entertainment furniture, wall units, chairs and sofas, ergonomic furniture and outdoor furniture are well received in Canada.

The Canadian household furniture industry has done well in the United States because of the elimination of duties on U.S.-origin products. The statistics have shown that the majority of the U.S. hardwood lumber exports to Canada are not being re-exported, as U.S. lumber is being used in Canada, either in its original form or as inputs for other (value-added or further manufactured) products.

Canadian Furniture Exports to the United States

Category	1995	1996	1997	1998	1999	2000	2001	2002
				$ Million				
Wooden Office	141	199	280	351	393	452	393	377
Wooden Kitchen	151	205	264	312	392	476	517	551
Wooden Bedroom	176	217	278	314	369	418	418	409
Total	468	621	822	977	1,154	1,346	1,328	1,337

Canadian Imports of U.S. Hardwood Lumber Have Climbed, Although the U.S. Share of the Total Market Has Dropped



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NAFTA: A Clear Success for U.S. and Mexican Textile and Cotton Trade

By Katherine Cook

NAFTA (the North American Free Trade Agreement) eliminated barriers for textile and cotton trade between Mexico and the United States. Ten years on, NAFTA has proven a great success for textile manufacturers on both sides of the border and for U.S. cotton producers.

Benefits for U.S. and Mexican Textile Industries

Since 1994, when NAFTA was first enacted, the textile industries in Mexico gained open access to the U.S. market, stimulating exports to the United States. The value of Mexican cotton textile and apparel exports to the United States increased from $3 billion in 1995 to $8.4 billion in 2002, with a record high of $9.4 billion in 2000. At the same time, Mexico's share of the U.S. cotton textile market rose from 8 percent in 1995 to 13 percent in 2002.

U.S. companies have benefited as well. NAFTA increased exports of U.S. yarn and cotton to Mexico in two ways. First, it eliminated import duties on U.S. yarn and cotton to Mexico. Second, to benefit from the reduced tariffs, NAFTA required Mexican textile manufacturers to use U.S. cotton and yarn for any U.S.-bound textile exports. As a result, all cotton textiles entering the United States from NAFTA countries contain U.S. cotton, while the same cannot be said of textile imports from other countries. U.S. exports of fabrics and yarn to Mexico increased from $1.1 billion to over $3 billion between calendar years 1995 and 2002.

The preferential treatment of U.S. yarn and fabric has been important to the struggling U.S. textile industry, which has suffered setbacks under low-priced imports from countries like Vietnam and China. It is likely that the cotton industry will look for similar requirements in future U.S. free trade agreements.

NAFTA's Benefits for U.S. Cotton

As NAFTA has fostered the growth of Mexico's textile industry, U.S. cotton exports to Mexico have seen a dramatic increase since 1994. In the 1994/95 marketing year (August-July), the United States exported a mere 580,000 bales of cotton to Mexico (1 bale=480 pounds), but by 2002/03, U.S. cotton exports to Mexico reached a record 2.3 million bales. NAFTA reduced the tariff on raw cotton exports to Mexico from 10 percent in 1994 to 5 percent in 1999. The tariff was phased out in January 2003. Preferential access for U.S. cotton in the Mexican market along with favorable rules of origin for textile product imports under the agreement have been key in supporting overall consumption of U.S. fiber.

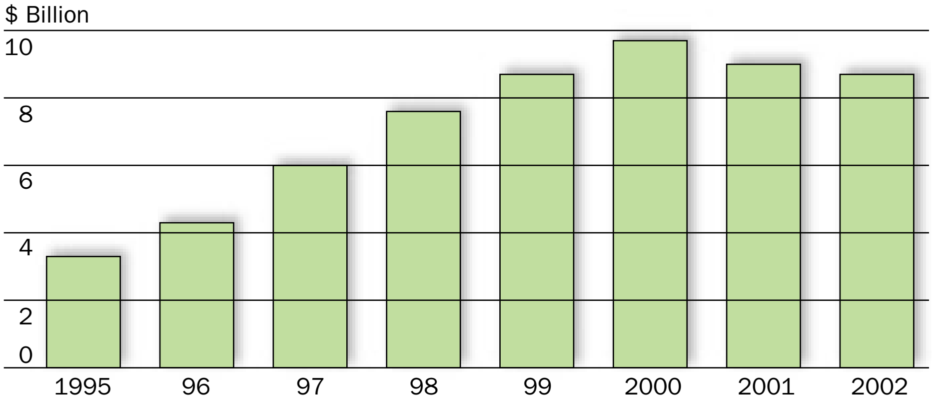
NAFTA's Future

While NAFTA's past performance in promoting textile and cotton trade has been impressive, there are challenges to its continued success. One challenge is increasing U.S. textile imports from China. Between 1997 and 2002, U.S. imports of cotton textiles and apparel from China increased from $7.2 billion to $9.8 billion, representing a 17-percent rise in market share.

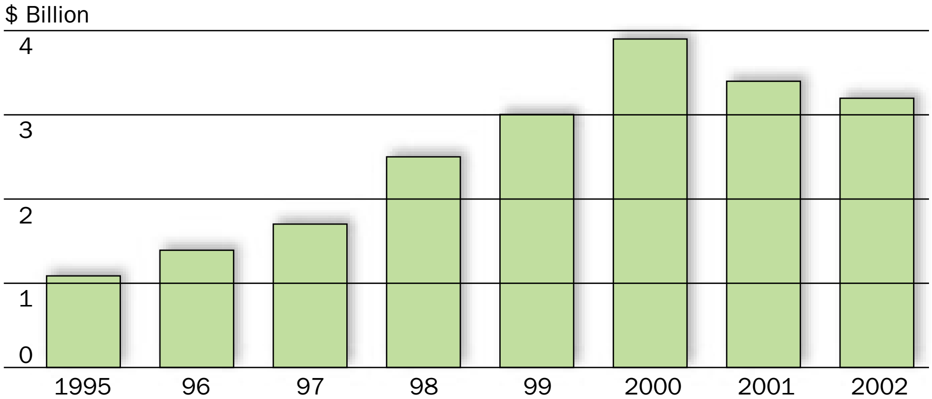
Another challenge is the final phase-out of textile quotas on Jan. 1, 2005 under the Uruguay Round agreement of the General Agreement on Tariffs and Trade, now the World Trade Organization. The elimination of quotas could potentially erode Mexico's share of the U.S. market, as competing countries can increase their textile exports to the United States. However, while losing the advantage of

NAFTA HAS PROVED A GREAT SUCCESS FOR TEXTILE MANUFACTURERS ON BOTH SIDES OF THE BORDER.

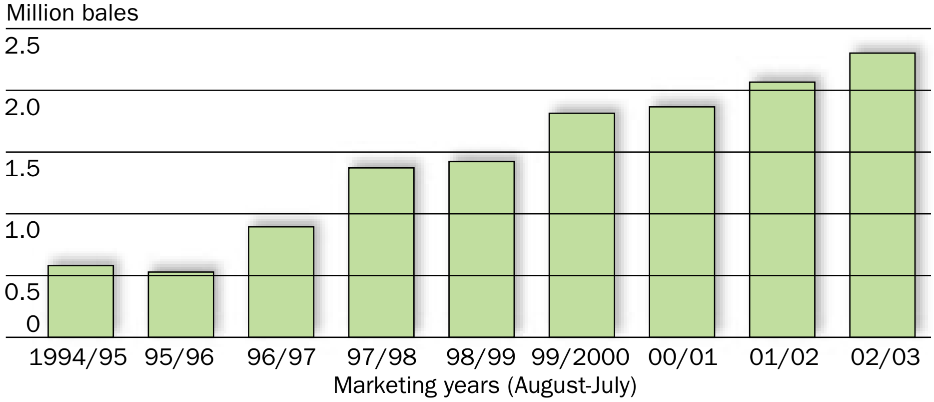
Under NAFTA, Mexican Textile Exports to the United States Have Climbed



U.S. Cotton Yarn and Fabric Exports to Mexico Have Made Impressive Gains



U.S. Cotton Exports to Mexico Have Surged



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quota-limited competition, Mexico will maintain a tariff advantage which allows 100 percent of all textile and apparel exports to enter the United States duty-free.

NAFTA's Success

Before NAFTA, both countries faced significant trade barriers in exporting to each other. NAFTA's elimination of these barriers for textile exports to the United States allowed Mexico to claim increasing shares of the U.S. market. At the same time, the United States was able to nearly quadruple its cotton exports to Mexico, claiming almost 100 percent of the Mexican cotton import market as Mexico's textile industry demand surged. U.S. cotton yarn exports also saw a dramatic rise as a result of NAFTA, with the total value of exports almost tripling between 1995 and 2002.

Without NAFTA, the exponential growth of U.S. cotton and cotton yarn exports to Mexico would likely have never materialized. The increases in textile and cotton trade between the United States and Mexico following NAFTA are a textbook example of the benefits of free trade. ■

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U.S. Wheat and Corn Exports to Mexico Thrive Under NAFTA

By Debbie Seidband

The U.S. grain sector has benefited in many ways from NAFTA (the North American Free Trade Agreement), and the outlook is favorable for continued expansion of grain trade between the United States and Mexico.

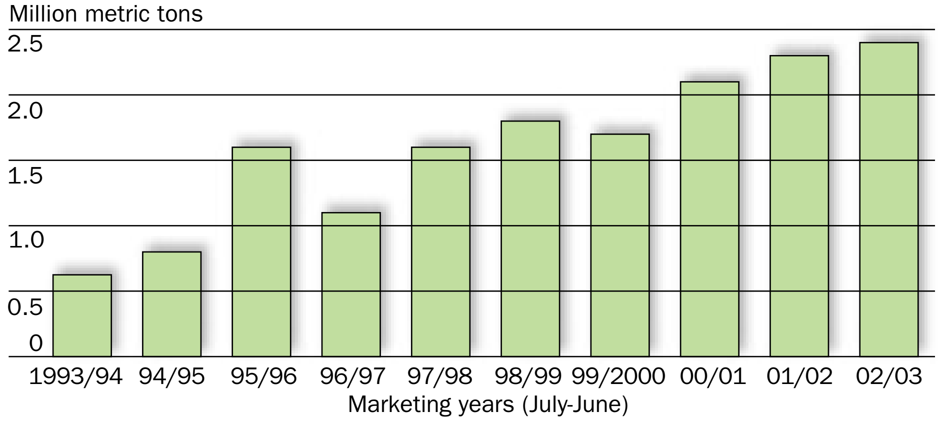
Before NAFTA, Mexico controlled all its grain imports through restrictive licensing and high tariffs. But now both the United States and Canada enjoy preferential treatment for their grain exports to Mexico.

Wheat Sweeps

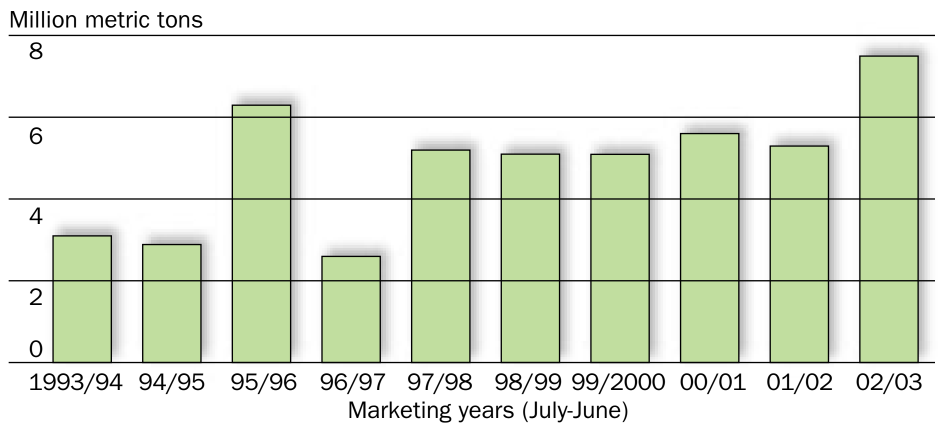
For example, Mexico's wheat import licensing requirement has been eliminated for the United States and Canada but remains in effect for all other suppliers, such as the European Union and Argentina. In addition, in 2003, Mexico's import tariff and TRQ (tariff-rate quota) for wheat was reduced to zero. The tariff on wheat from other suppliers stands at 67 percent, effectively shutting them out of this market.

In marketing year 2002/03 (July-June), the United States supplied 2.4 million metric tons out of the total 3.2 million tons of wheat imported by Mexico. In the year prior to NAFTA, U.S. market share in the Mexican wheat market was approximately 56 percent. As a result of lower tariffs and increasing quota levels, the United States has increased its market share to 75 percent since the inception of NAFTA in 1994.

Under NAFTA, U.S. Wheat Exports to Mexico Have Grown Nearly Fourfold



U.S. Corn Exports to Mexico Have More Than Doubled



Corn a Bestseller

Mexico consistently ranks as the second or third largest market for U.S. corn, buying virtually 100 percent of its imports from the United States. Mexico has set a TRQ with a zero duty for corn of U.S. or Canadian origin. Since 1994, the quota has increased 3 percent each year, starting at 2.5 million tons and currently at 3.26 million tons.

Despite Mexico's recent enforcement of the minimal duties on the over-quota amount, the country continues to regularly import one-and-a-half to nearly two times its TRQ amount due to industry demand. Mexican import demand for corn in marketing year 2003/04 is projected to reach a record high of 7.5 million tons, boosted by heightened demand from the Mexican livestock and starch industries. ■

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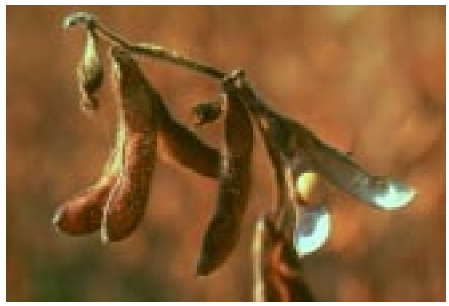
NAFTA Contributes to Growth in U.S. Soybean Exports to Mexico

By Alan Hallman

U.S. soybean exports to Mexico have grown at a tremendous rate since the implementation of NAFTA (the North American Free Trade Agreement). In the last nine years, U.S. soybean sales to Mexico have increased by more than 125 percent, and Mexico has become the third largest market for U.S. soybeans.

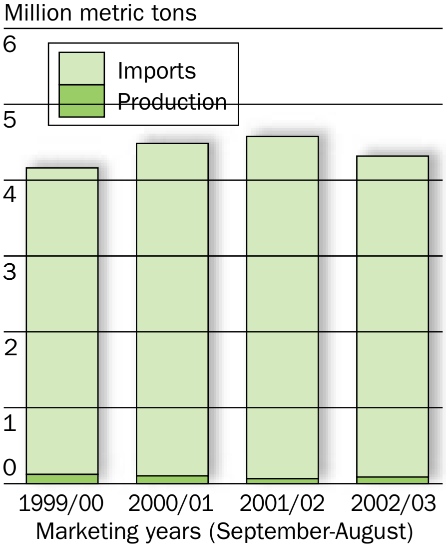
NAFTA encouraged expansion of Mexico's livestock production and modernization of its oilseed crushing industry. Despite an economic slowdown, crushing capacity continues to grow, boding well for U.S. soybean exports to Mexico.

When NAFTA was first implemented, the Mexican oilseed industry was striving to meet the protein requirements of a growing livestock sector with declining domestic oilseed production. By 1994, Mexico's soybean production had fallen by nearly 50 percent to an estimated 500,000 metric tons, down from a high of about 1 million tons in 1989.

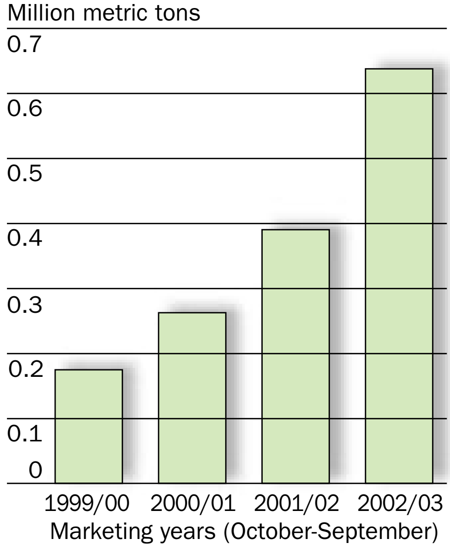


NAFTA provided Mexico with improved access to U.S. soybean supplies for their growing livestock industry. This access, combined with Mexico's close proximity to the United States, has helped to solidify the U.S. position as the dominant supplier of soybeans to Mexico.

Mexico's Soybean Supply is Made Up Mostly of Imports



Mexican Soymeal Imports Have Risen



U.S. Soybean Market Share Threatened by Tight Supplies

The second short U.S. soybean crop in as many years has increased soybean prices and may provide an opportunity for South American producers to gain market share in Mexico. Current projections are for Mexican soybean imports to rise by 4 percent to 4.4 million tons in marketing year 2003/04, while U.S. soybean exports to Mexico remain at 2002/03 levels. While high prices will restrain consumption growth, continued expansion in the poultry industry and more integration in the swine sector should lead to higher Mexican soybean meal consumption in 2003/04.

The growth rate of U.S. soybean exports to Mexico has slowed from an average of almost 16 percent in the four years after the inception of NAFTA, to a still impressive average growth rate of 5.4 percent over the past five years. While U.S. soybean meal exports to Mexico have been smaller than soybean exports, trade in soybean meal has started to grow very rapidly. U.S. soybean meal exports to Mexico increased 59 percent in 2002 and are estimated to have grown another 52 percent in 2003.

In marketing year 2002/03 (September-August), U.S. soybean exports to Mexico totaled 4.1 million tons, valued at $911 million. The United States provides Mexico with about 98 percent of its soybean imports, and all of its soybean meal imports. ■

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NAFTA Spells Success for Consumer-Oriented Products—With Some Reservations

By Joani Dong

Since NAFTA (the North American Free Trade Agreement) implementation began on Jan. 1, 1994, export sales of U.S. consumer-oriented products to Canada have soared, reaching $6.1 billion in calendar 2002, while sales to Mexico have leaped to $2.8 billion.

In 2002, U.S. consumer-oriented products made up the lion's share of all U.S. agricultural exports to Canada (70 percent) and Mexico (39 percent). Duty-free entry for most products has sparked sales, and so have lifestyle changes in Canada and Mexico that parallel trends in the United States: increased income, less free time, emphasis on convenience, more women working outside the home and more pet ownership.

Under NAFTA, just about every item in the U.S. consumer-oriented category experienced sales increases to both Canada and Mexico. U.S. dried soup to Mexico is a case in point, with sales in 2002 at $198 million, a whopping tenfold increase from 1993, the year before NAFTA began to take effect. This gain reflects the growing importance of convenience to consumers and growth of Mexico's restaurant and tourism industries.

Pet food exports to Mexico tell another success story. Between 1994 and 2001, U.S. exports of dog and cat food climbed from $30 million to $235 million, although they declined in 2002. Mexico's import market for pet food is one of the fastest growing segments in one of the fastest growing markets in the world, and the United States has more than a 95-percent share of it. Domestic production is increasing, but not enough to meet demand. Increasing per capita income has led to more pets per household, particularly in urban areas. Aggressive marketing campaigns and more visits to veterinarians have prompted Mexican pet owners to switch from table scraps to commercial pet foods.

From the Horse's Mouth

Here is a sampling of activities and experiences under NAFTA from state-regional trade groups and trade associations that work closely with FAS to promote U.S. agricultural exports.

The Mid-America International Agri-Trade Council and **Food Export USA** have engaged in a number of activities, such as conducting trade missions, arranging one-on-one meetings with U.S. companies and top retailers and organizing supermarket tours and displays. Companies participating in the cost-share branded program have steadily increased their sales. For instance, **Palermo's Villa**, a small family-owned pizza company, got such a positive response in the Canadian market through in-store promotions and samplings that it has had to expand facilities to meet demand.

The Western United States Agricultural Trade Association promoted western fruits and vegetables through in-store promotions with over 100 Soriana supermarkets in Mexico. Sales of promoted items reached a robust $907,000 in 2003, with an investment of only $14,650 in marketing funds. **The Perfect Puree of Napa Valley** line of Hayward Enterprises, Inc., was included in a five-day pastry course at the Maricu Culinary Arts Center in Mexico City, resulting in purchases by discriminating French chefs in first-class Mexican hotels.

The Southern United States Trade Association has found ways to benefit its member states through Go South!, an umbrella branding program to promote quality produce in Canada. The program promotes 19 commodities from 16 southern states through media and trade relations, in-store promotions and consumer information. Shipments of the 19 commodities promoted by Go South! have increased from 136 million pounds in 1996 to 206 million pounds in 2001. In 2002, while Mother Nature put a damper on many southern crops, shipments still reached 158 million pounds.

The Louisiana Department of Agriculture and Forestry cites two examples of the rewards and difficulties companies in the state have had under NAFTA. A Louisiana meat packer successfully conducted business for 2-3 years in Mexico and created solid business relationships. Orders from restaurant chains and resort hotels were good. Payments were punctual, and there were no significant export problems. Nevertheless, its business was interrupted when the Mexican government began charging small and medium-sized packers higher fees than the largest packers.

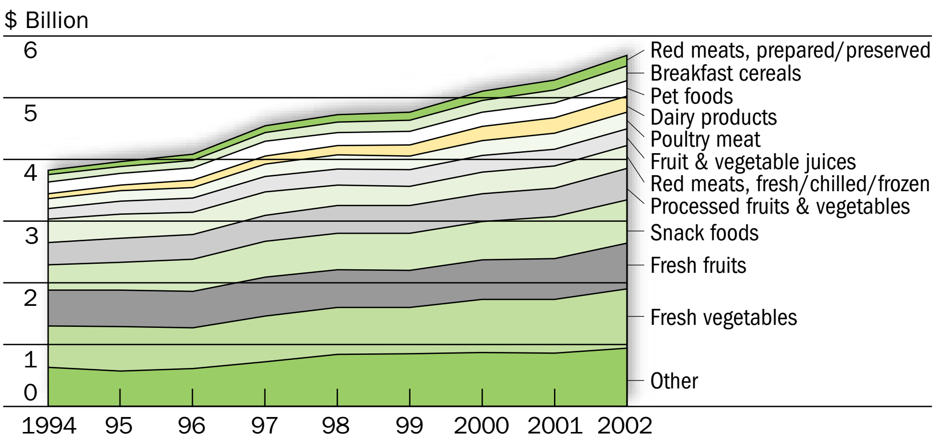
In another example, some Louisiana companies participated in display promotions with supermarket chains such as Carrefour and Wal-Mart, but found that the promotions did not lead to subsequent orders. The lesson here is that companies must follow through with further investments in publicity, demonstrations and other activities.

All companies need to know the particulars of their specific target markets, i.e, sanitary issues, labeling rules, other market requisites and cultural differences in conducting business.

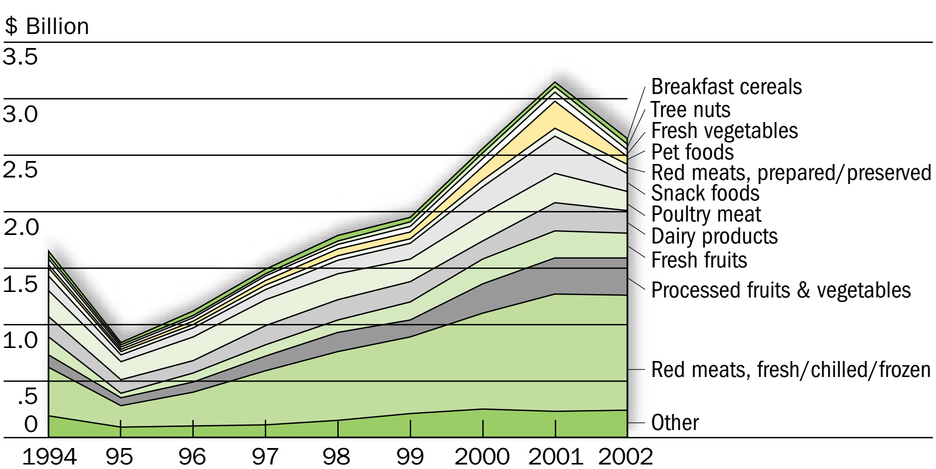
USAPEEC (the USA Poultry and Egg Export Council) experienced success of another kind. USAPEEC worked with its counterpart industry organization in Mexico, Union Nacional de Avicultores, to address issues that could have led to disruptions in poultry trade. The two groups and the U.S. and Mexican governments agreed to extend the tariff-rate quota transition period for leg quarters through 2008, and eliminate a number of excessive sanitary import requirements, to keep trade flowing. U.S. total broiler meat exports to Mexico are forecast to grow steadily through 2012 unimpeded by unnecessary sanitary import requirements.

Mexico has become the leading market for U.S. turkey exports and the second largest market for U.S. chicken. In fact, more than 90 percent of all sausage and deli meats produced in Mexico contain U.S. poultry ingredients, such as mechanically de-boned poultry meat and boneless turkey cuts.

Under NAFTA, U.S. Consumer-Oriented Product Exports to Canada Have Shown Substantial Broad-Based Growth...



...As Have U.S. Consumer-Oriented Product Exports to Mexico



Some Reservations Remain

Trade successes aside, there are still reservations. The National Food Processors Association represents the $500 billion food processing industry on scientific and public policy, food safety, nutrition, technical and regulatory matters and consumer affairs. Most of the association's 400 member companies depend on Mexico for raw materials and for markets for their finished products.

However, the association states that nontariff barriers for processed food exports to Mexico are significant, such as complex documentation and registration requirements for entry; inconsistent border procedures that result in rejections; excessive inspections; and costly detention of products for minor paperwork infractions. Mexico also requires expiration dating on all processed products, rather than the "best before" dating that is a more useful indicator of safety and quality. Temperature control throughout the distribution chain is a significant problem.

In addition, Mexico has imposed product conformity standards (standards of identity) that block several U.S. products from the market due to restrictive limitations on food additives and flavorings. Moreover, export certification requirements are restrictive for products that contain fresh, frozen and processed meat ingredients derived from ruminants.

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OLYMPIC TRADE MISSION

GREECE TRADE MISSION

What: FAS is sponsoring a trade mission to Athens, Greece that will provide a unique opportunity to learn first-hand about the Greek market for U.S. food products in a concise, informative program. Since Greece is hosting the 2004 Summer Olympic Games, tourism increases will lead to an urgent need for imported food.

Participants will learn about food service opportunities from Olympic Organizing Committee representatives. They will tour wine stores, catering facilities and supermarkets, and have one-on-one meetings with qualified buyers. In 2002, a similar mission generated over $4 million in sales for participating companies. Space is limited to 10 participants. Eligible expenses are reimbursable through the branded initiative of the Market Access Program, administered by FAS, commodity organizations and state-regional trade groups.

When: March 28-April 1, 2004

Where: Athens, Greece

The Market: Greece is an import-dependent country with a population of 11 million, and the world's 15th most popular tourist destination. During 2004, tourism is expected to more than double to 25 million visitors. During the 17 days of the Olympics, more than 11.5 million meals will be served at Olympic facilities alone. This figure does not include the additional restaurant meals or ready-to-eat foods purchased at supermarkets.

Greeks' disposable incomes are growing. U.S. foods are popular and regarded as high quality. In 2002, Greece imported almost $40 million in U.S. consumer-ready foods, up 7 percent from 2001.

Best Products: Nuts, frozen foods (vegetables and convenience foods), seafood, snack foods (salty and sweet), wines, beer, meats and edible dried pulses (lentils, beans and peas)

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Trade Notes...

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USDA Grants Assistance to Three Groups Under Trade Adjustment Assistance

In October, FAS announced that producers of wild blueberries in Maine, and salmon fishermen in Washington and Alaska, were eligible to apply for benefits under the TAA program (Trade Adjustment Assistance for Farmers). Under the TAA program, USDA provides technical assistance and cash benefits to producers if an increase in imports of a like commodity has contributed importantly to a decline in price and a loss of income. After receiving petitions from the Wild Blueberry Commission in Maine, Puget Sound Salmon Commission in Washington, and United Fishermen of Alaska, FAS determined that imports contributed importantly to a decline in the domestic price of these products in the respective states. After producers submit completed applications, technical assistance and training will begin as soon as possible. Financial payments will not be made until after applications are certified. For further information about the TAA program, contact Jean-Louis Pajot, Coordinator, Trade Adjustment Assistance for Farmers, FAS, USDA. Tel.: (202) 720-2916, E-mail: trade.assistance@fas.usda.gov

ATO Shanghai Launches First Western China Wal-Mart American Food Festival

In October, the Wal-Mart American food promotion opened concurrently at two supercenters in Kunming, the capital of Yunnan province in China. The Washington State Agricultural Trade Association, Alaska Seafood Marketing Institute, U.S. Meat Export Federation, Almond Board of California, U.S. Potato Board, California Pistachio Commission and many U.S. food distributors participated in the promotion. A total of 155 U.S. food products, including 44 new-to-market items, were featured. Internationally famous pastry chef Eric Perez led a hands-on baking seminar featuring recipes using dried fruits and nuts. Initial reports from the promotion indicate brisk sales of pistachios, almonds, V8 vegetable juice, Post cereals, Kraft Miracle Whip, bakery products, Lamb-Weston frozen potato fries, Washington apples, prunes and table grapes.

$11 Million Projected in 12-month Sales at ABASTUR 2003

In October, FAS sponsored a USA Pavilion at ABASTUR, the largest hotel and restaurant trade event in Mexico. In the USA Pavilion, 38 exhibitors reported 1,024 serious business contacts, $201,900 in onsite sales and $11.2 million in projected 12-month sales. Products that generated the most interest were poultry, honey, fully cooked bacon, deli meats, yogurt, cottage cheese, wines, dried fruits, cheesecake, brownies, potato fries and frozen soup products.

World Food Moscow Results in $1.9 Million in Sales

In September, 26 U.S. companies exhibited in the USA Pavilion at Russia's World Food Moscow. Exhibitors reported that they expect sales of $1.9 million worth of processed foods over the next year as a result of the show. Forty-nine products were introduced and tested in the Russian market. Russian importers and distributors got to sample nuts, dried fruits, almonds, wines, pears, apples, cocoa, vegetables, seafood, meat products and other items.

TRADE SHOW OPPORTUNITY

FOOD & HOTEL ASIA 2004

SINGAPORE

The Market:

Economically and industrially, Asia is the world's fastest growing region. Asia has more than one-half of the world's population, which is projected to grow 44 percent over the next 50 years.

Singapore is at the hub of Southeast Asia, which is comprised of the Philippines, Indonesia, Malaysia, Thailand, Vietnam, Laos, Burma, Brunei and Cambodia. The region has a combined population of 500 million people. These culturally rich and politically diverse countries offer opportunities to a wide range of U.S. food exporters. In calendar year 2002, the region imported $670 million worth of U.S. consumer-oriented agricultural products.

Key buyers from countries well beyond Southeast Asia—such as India, South Korea, Australia and Japan—attend Food & Hotel Asia looking for new products. In fact, over 33,000 international buyers from 99 countries attended Food & Hotel Asia 2002.

Dates:

April 20-23, 2004

Why:

Singapore is one of the most efficiently run countries in the world, well-served by air, sea and telecommunications. In this business-oriented country, you can reach buyers from all corners of the world. Many exhibitors consider Food & Hotel Asia to be Asia's best food show, due to its high number of international visitors.

At Food & Hotel Asia 2004, you will find thousands of buyers from hotels, restaurants, fast-food/quick-service outlets, supermarkets, hypermarkets, grocery stores, food and drink importers, wholesalers, distributors and purchasing officers for the industrial catering sector.

Best Prospects:

Fresh produce, chilled and frozen foods, meats and poultry, confectionery items, snack foods, ice cream and other dairy products, seafood, specialty foods, ingredients, beverages, processed and convenience foods

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TRADE MISSION

MALAYSIA TRADE MISSION

What: FAS is sponsoring a trade mission to Kuala Lumpur, Malaysia, directly after Food & Hotel Asia 2004 in Singapore. It will provide a unique opportunity to learn first-hand about Malaysian markets for U.S. food products in a concise, informative program. Participants will tour local street markets and supermarkets, as well as have one-on-one meetings with qualified buyers. In 2002, a similar mission generated over $2 million in sales for participating companies. Space is limited to 10 participants. Eligible expenses are reimbursable through the branded initiative of the Market Access Program, administered by FAS, commodity organizations and state-regional trade groups.

When: April 24-27, 2004

Where: Kuala Lumpur, Malaysia

The Market: Malaysia, with a population of 24.5 million people, is one of Southeast Asia's most developed nations. About 61 percent of its population falls in the middle- to upper income group of consumers. Its economy has a firm foundation with strong manufacturing, service and agricultural sectors. The Malaysian economy is estimated to have grown by 4.5 percent in 2003 and forecast to grow 5.5 to 6 percent in 2004.

The Malaysian food and beverage market is becoming increasingly sophisticated and includes both local and imported products. The strong economic growth in the late 1980s and early 1990s has contributed to major changes in consumer purchases and consumption patterns. In 2002, Malaysian imports of consumer-oriented agricultural products from all sources were about $143 million, with fresh fruits, processed fruits and vegetables and snack foods leading the way.

Best Products: Fresh fruits and vegetables, snack foods and nuts, wines, dairy products, halal meats and preparations, products for food service

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Inside This Issue:

- NAFTA's impact on overall trade trends, investment and market integration, and successes and challenges
- NAFTA experiences in Mexico and Canada
- NAFTA's influence on trade in selected products

And Next Time, Turn to AgExporter for:

- Austria's market for organic products
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NAFTA 10

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